# Contracting in India: Effectively Executing Commercial Contracts


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# General principles of contracts

- India’s legal system is largely based on the common law system. Principles governing contracts are similar to those prevalent in the UK.

- The Indian Contract Act, 1872 (“**Contract Act**”) regulates contracts in India. Contracts may be written or oral, although oral contracts are difficult to prove.

- There are no statutory restrictions regarding choice of law of the contract.

- If one of the contracting parties is a foreign national/entity, parties may expressly agree to any governing law, provided, the choice of foreign law does not violate India’s public policy.

- Foreign law must be proved in Indian courts in the same manner as any other evidence.

- Choice of forum clauses should be carefully considered. A foreign court decree can be enforced in India if it is of a superior court from a reciprocating territory.

- US is not a reciprocating territory under India’s civil procedure code. If a US court decree is sought to be enforced in India, a fresh suit will have to be filed before a competent Indian court.

- Parties should consider resolving disputes by way of arbitration as arbitral awards passed in the US are easily executable and enforceable in India under the New York Convention.

# General principles of contracts (Contd.)

- Under the Contract Act, the essential elements of a valid contract are as follows:
    - Free consent;
    - Parties competent to contract;
    - Lawful consideration; and
    - Lawful object.
- Contracts executed on the basis of consent caused by coercion, undue influence, fraud or misrepresentation are voidable at the option of the party whose consent is caused or taken by coercion, undue influence, fraud or misrepresentation.
- If both parties are mistaken as to an essential fact, the contract can be void.
- Agreements in restraint of legal proceedings are invalid.
- Agreements that seek to reduce the statutorily prescribed limitation period and agreements that bar the jurisdiction of civil courts by mandating an in-house dispute resolution mechanism (except arbitration) are examples of agreements that can be held to be void.

# Restrictive covenants

- Restrictive covenants can be used in employment contracts to prevent employees from:
  - Starting a competing business;
  - Working for a competitor;
  - Soliciting one’s customers;
  - Recruiting one’s current employees; and
  - Disclosing trade secrets or confidential information.
- Non-compete and non-solicit (relating to customers) clauses are generally enforceable during the term of the contract, especially in employment contracts.
- Such clauses may not be enforceable post-termination but can be retained as a deterrent.
- Non-solicit (relating to employees), non-disclosure and non-disparagement clauses are generally enforceable.

# Protecting confidential information

- No specific law in India protects trade secrets or confidential information.
- Indian courts have granted injunctions to protect confidential information on the principles of equity and common law.
- Prevalent in employment contracts, investment transactions and joint venture agreements.
- Remedies can include either temporary or permanent injunctions to protect the information in addition to damages and other contractual remedies.
- Excluded Information:
  - Information which is in the public domain;
  - Information which becomes available to the public without a breach of the contract; and
  - Information which a party obligated to disclose pursuant to any law, regulatory regime or a judicial body.

# Dispute resolution

- Commercial courts in certain jurisdictions are prompt and commercially savvy. However, court proceedings can also get long-drawn and expensive.
- Parties should choose to resolve their disputes through binding arbitration.
- Parties should retain the right of seeking injunctive relief from a competent Indian court.
- Remedies for breach of contract
  - Litigation:
    - ✓ Injunctive relief - Interlocutory and permanent reliefs are available.
    - ✓ Damages.
  - Alternate Dispute Resolution:
    - ✓ Damages
    - ✓ Arbitrators are empowered to grant interim reliefs and specific performance of contractual obligations.

# Limitation of liability

- Generally, liability for breach of contract is attributed to the party committing the breach.
- Parties to a contract may restrict their liability by including an express provision to that effect in the contract.
- Limitation of liability clauses may be struck down if found to be unconscionable in nature.
- Such clauses may also be held to not be operable where a loss is caused due to a fundamental breach of the contract.
- Instances where Indian courts have refused to enforce limitation of liability clauses include:
  - Clauses that bar a party from claiming damages that such party would otherwise be entitled to under law.
  - Breaches of contract that are caused due to gross negligence or fraud.
  - Breaches that affect the core or root of the contract.

# Indemnification

- Features of an Indemnity clause:
  - Include claims arising from actions of third parties; and
  - May be claimed before the loss has actually been incurred but after the loss is suffered.
- Effective May 20, 2016, caps have been imposed on deferred consideration and indemnity pay outs in a cross-border share sale transaction.
- Reserve Bank of India (RBI) approval needed if the following limits are exceeded:
  - consideration amount deferred or escrowed exceeds 25% or a period of 18 months from the date of the transfer agreement; and
  - seller's indemnity exceeds 25% of the total consideration or a period of 18 months from the date of payment of the full consideration.

These caps warrants a thorough due diligence to be done on the seller entity backed with representations and warranty insurance.

# Due Diligence

- Conducting an extensive due diligence is extremely important when considering the acquisition of an Indian entity.

- A legal due diligence typically involves review of documents in person or shared in a secure virtual data room.

- Site visits may be required for EHS, operational and other forms of due diligence.

- <u>Typical due diligence issues</u>

  - Improper maintenance of corporate, employment and other records;
  - Inadequate intellectual property protection;
  - Lack of statutory compliances;
  - Environmental law non-compliance for manufacturing concerns;
  - Anti-corruption/ bribery issues; and
  - Data privacy related issues.

# Damages

- Liquidated damages (specific sums pre-agreed upon by parties) and unliquidated damages can be awarded.
- <u>Pre-requisites for a damages claim</u>
  - Direct nexus with a breach;
  - Foreseeable consequence;
  - Damages arise in the usual course of things; and
  - Cannot be aggravated damages.
- Agreed liquidated damages may also be limited by courts to the reasonable or actual compensation for injury/damage sustained.
- In certain situations, parties may also claim anticipatory damages on account of an anticipatory breach of the contract.
- Typically, any indirect, special, consequential or punitive damages are not permitted to be recovered, and only direct losses can be recovered in case of breach of a contract.

# Employment law - Key considerations

- Employment laws include Central laws and State-specific legislations.
- Mandatory requirements on leave, holidays, facilities and benefits to be provided by employer, and prevention of sexual harassment.
- Factors to determine applicability of employment laws
  - Nature of business and number of employees;
  - Location of the employer and employee; and
  - Role, responsibilities and salary of employee.
- At-will termination of employees not in a managerial or supervisory capacity is not possible.
- Importance of employment contracts
  - Restrictive covenants and confidentiality obligations;
  - Benefits to managerial/supervisory employees; and
  - Assignment of intellectual property.

# Forms of hiring arrangements

- Employment arrangements
  - Employer-employee relationship is comparable with a master-servant relationship.
  - Employer is required to comply with employment laws and provide statutory benefits.
- Independent contractor arrangements
  - Employer-independent contractor relationship is comparable with a principal-agent relationship.
  - Employer is not required to comply with any employment laws.
  - Personal tax planning can get more efficient for Independent contractors
- Outsourcing arrangements
  - Employer and a contractor/agent enter into a contract for hiring personnel and there is no direct contract between the employer and employee.
  - Employer is required to comply with the Contract Labour (Regulation and Abolition) Act, 1970.

# Anti bribery compliance

- The Prevention of Corruption Act, 1988 (“**POCA**”) is the key legislation on anti corruption. POCA covers only government officials (public servants).

- <u>Some differences between POCA and Foreign Corrupt Practices Act, 1977</u>:

  - POCA criminalizes giving and accepting a bribe;

  - No requirements on due diligence and compliance programs to mitigate violations;

  - No concept of grease money; and

  - Financial penal implication not very significant - imprisonment between 6 months and 5 years, and a fine.

- <u>Key compliance measures</u>

  - Adopt manuals/guidance notes on anti-bribery compliances and reporting;

  - Educate and encourage employees to report any breaches of anti-bribery policies/laws; and

  - Conduct post-training assessment to validate the understanding of the employees, business partners and associates, agents, and distributors.

# Execution formalities

- <u>Electronic Signatures</u>

  - A  digital signature certificate, which is issued by certifying authorities in India, can be used but it is different from DocuSign and other electronic signatures.

  - A digital signature certificate is only valid for electronic records and not for scanned or printed copies of documents.

  - Electronic signatures other than digital signature certificates cannot be used to authenticate documents. Wet ink signatures are preferred.

  - Signatures can be exchanged by e-mail, followed by exchange of originals, if the agreement so provides.

- <u>Stamp Duty</u>

  - Stamping of documents is a process through which the Indian government collects tax on commercial and non-commercial transactions in India.

  - Amount of the stamp duty payable on an instrument is typically determined as per the laws applicable in a particular State.

# Execution formalities (Contd.)

- To ensure that parties do not evade this tax, Indian law disallows the admissibility of documents as evidence which have not been adequately stamped.

➢ Registration

- It is a process by which certain documents are presented before an Indian authority to enable the creation of a public record for such documents.
- As a general rule, registration of documents is mandatorily required only for documents that create or extinguish rights in respect of an immoveable property.
- Typically, registration requires all signatories and witnesses to an agreement to be personally present for the registration process.

# Thank You


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